MCI WORLDCOM 1801 Pennsylvania Avenue, NW
Washington, DC 20006

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Larry Strickling
Chief
Common Carrier Bureau
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

August 20, 1999

Re: CC Docket No. 96-98 and CC Docket No. 95-185

Dear Mr. Strickling:

Several incumbent local exchange carriers have filed ex parte submissions in these dockets arguing that CLECs should be prevented from using extended link for the provision of exchange access services. Enclosed with this letter is a legal analysis that demonstrates that CLECs may purchase extended loops solely to provide exchange access services.

If you have any questions about this submission, please feel free to contact me.

Sincerely,

Chuck Goldfarb

Chuck Goldfarb
Director
Law and Public Policy

Enclosures

cc. Jake Jennings
Christopher Libertelli
Carol Mattey
Claudia Fox

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Lisa B. Smith
Senior Policy Counsel
Local Markets and Enforcement

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OFFICE OF THE SECRETARY

August 20, 1999

EX PARTE

Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, S. W.
Washington, D.C. 20554

Re: In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; CC Docket No. 96-98

Dear Ms. Salas:

On behalf of MCI WorldCom, Inc., enclosed is an ex parte that was submitted to Larry Strickling, Chief, Common Carrier Bureau. MCI WorldCom requests that this ex parte be entered into the record for the above-referenced docket.

In accordance with Section 1.1206(b)(2) of the Commission's Rules, an original and one copy of this notice are being submitted to the Secretary.

Sincerely,

Lisa B. Smith
Senior Policy Counsel

cc: Larry Strickling
Carol Mattey
Jake Jennings
Claudia Fox
Christopher Libertelli

MCI WORLDCOM
1801 Pennsylvania Avenue, NW
Washington, DC 20006

EX PARTE OR LATE FILED

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Larry Strickling
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445 12th Street, SW
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Chuck Goldfarb

Chuck Goldfarb
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Law and Public Policy

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RESTRICTING THE USES OF EXTENDED LINK

The suggestions of several Bell Operating Companies (BOCs) to the contrary notwithstanding,[1] the Federal Communications Commission (Commission) has no legal authority to prevent competitive local exchange carriers (CLECs) from using extended link for the provision of access services. Even if the Commission did have the authority to impose such restrictions, they would further no legitimate purpose and would impede the development of competition in all telecommunications markets. As section 251(d)(2)(B) of the Telecommunications Act imposes no limits on the kinds of telecommunications services CLECs may offer through network elements the Commission determines should be unbundled, BellSouth's suggestion that this provision supports its view that the Commission may limit the uses to which unbundled elements are put is without merit. Once the Commission has determined that CLECs are impaired in their ability to offer the services they seek to offer without access to an element, section 251(c)(3) of the Act requires incumbent local exchange carriers (ILECs) to provide unlimited access to that unbundled network element for all telecommunications purposes. Nothing in the Supreme Court's decision in Iowa Utilities Board calls into question the Commission's previous judgment that section 251(c)(3) must be construed to allow CLECs to use unbundled network elements for all telecommunications purposes.

I. The BOCs' Limited Use Proposal Is Unlawful.

As the Bell Companies acknowledge, the Commission has squarely held that

> section 251(c)(3) permits interexchange carriers and all other requesting telecommunications carriers, to purchase unbundled elements for the purpose of offering exchange access services, or for the purpose of providing exchange access services to themselves in order to provide interexchange services to consumers.

[1]See August 11, 1999, ex parte letter in CC Docket No. 96-98 from SBC Corporation to Lawrence E. Strickling, with accompanying legal memorandum, and August 9, 1999 ex parte in CC Docket No. 96-98 from BellSouth Corporation to Lawrence E. Strickling.

First Report and Order, In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, 11 F.C.C.R. 15499, ¶ 356 (1996) ("Local Competition Order"). The Commission stressed that " we believe that our interpretation of section 251(c)(3) . . . is compelled by the plain language of the 1996 Act . . . [since] section 251(c)(3) provides that requesting telecommunications carriers may seek access to unbundled elements to provide a 'telecommunications service,' and exchange access and interexchange services are telecommunications services." Id. (emphasis added).

The BOCs do not ask the Commission to reconsider this conclusion.[2] Instead they make two legal arguments in support of their proposed restrictions. Both claims are without merit.

First, BellSouth (but not SBC), suggests that in the Local Competition Order the Commission addressed only the situation in which a CLEC uses a UNE for both access and telephone exchange traffic, and that different considerations ought to apply when considering whether CLECs can use UNEs exclusively for access traffic. Ex Parte at 4. But this is not so. As the above-quoted portion of its Order makes clear, in the Local Competition Order the

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[2]The BOCs do advance several legal arguments the Commission rejected in reaching its conclusion. First, the BOCs note that section 251(c) allows ILECs to impose "just" and "reasonable" terms and conditions upon access to network elements. But since the statute expressly provides that leased elements can be used to provide all "telecommunications services," including exchange access services, plainly it would be neither just nor reasonable within that statutory scheme to limit use to only certain telecommunications services. Next, the BOCs argue that such restrictions are necessary to preserve the existing access charge regime, and that section 251(g) compels that this regime be preserved until replaced with another regime. As to that, the Commission has already concluded that this provision applies to ILEC exchange access services, and not to the new leasing requirements of the Act, and that in particular "this provision does not apply to the exchange access 'services' requesting carriers may provide themselves or others after purchasing unbundled elements." Local Competition Order ¶ 362. And, finally, the BOCs argue that section 252(i), which preserves the Commission's regulatory authority to set rates for services under section 201, preserves the Commission's right to impose restrictions on leasing. As to this as well, the Commission has already reached the contrary conclusion, finding that "our authority to set rates for these services is not limited or affected by the ability of carriers to obtain unbundled elements for the purpose of providing interexchange services." Id. ¶ 358.

Commission considered and rejected the same proposal the BOCs make in their ex partes: that CLECs can be prevented from using UNEs for the sole purpose of originating and terminating exchange access traffic. In suggesting the contrary, BellSouth relies on the Commission's observation that the risks of arbitrage of which the BOCs complained are minimal, since most customers use their phone lines for both local and long distance traffic. This was not, however, stated as a limitation on the rule that CLECs had the absolute right to determine which telecommunications services to offer over leased elements, but rather as an explanation as to why there was no need for any such limitation. See, e.g., Local Competition Order ¶ 357 ("interexchange carriers purchasing unbundled loops will most often not be able to provide solely interexchange services over those loops") (emphasis added).[3]

Second, although the BOCs acknowledge that the "no limitation on UNE use" rule is compelled by statute, they insist that the Commission retains authority under sections 201(b) and 154(i) to implement a temporary transitional rule that imposes just such limitations. In this regard, they observe that the Commission imposed such a transitional rule imposing non-cost-based "access" charges in the Local Competition Order, and that the Eighth Circuit upheld the

[3]In its ex parte, BellSouth misconstrues the Commission's Order on Reconsideration, In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, 11 F.C.C.R. 13042 (1996) ("Order on Reconsideration"), in the same way it misconstrues the Local Competition Order. See Ex parte at 4-5. In that Order, the Commission observed that the unbundled local switching element includes a switch line port that is dedicated to a particular customer loop. See Order on Reconsideration ¶ 11. Since, "as a practical matter," Order on Reconsideration ¶ 12, most customers need their loops for both local and long-distance service, the Commission in its Order on Reconsideration simply "ma[d]e clear that, as a practical matter, a carrier that purchases an unbundled switching element will not be able to provide solely interexchange service or solely access service to an interexchange carrier." Id. ¶ 13. Since the line port is part of the unbundled local switch, and since a customer's switched traffic includes both local and long-distance traffic, CLECs that make use of ILEC unbundled local switching will be switching both local and long-distance traffic.

Commission's right to impose such a transitional rule. See Competitive Telecommunications Association. v. FCC, 117 F.3d 1068, 1073-75 (8th Cir. 1997) ("Comptel").

Comptel cannot bear the weight the BOCs place on it. Simply put, the Commission has no authority to promulgate regulations contrary to express statutory provisions. See 47 U.S.C. § 154(i) (the Commission "may perform any and all acts . . . not inconsistent with this Act"); United States v. Storer Broadcasting Co., 351 U.S. 192, 201 (1956) ("§ 154(i) . . . grant[s] general rulemaking power not inconsistent with the Act or law"). Here, as the Commission has determined, section 251(c)(3) of the Act mandates that interexchange carriers must be allowed to purchase unbundled network elements for any purpose, including the purpose of offering interexchange services. Local Competition Order ¶ 356. The Commission has no authority to ignore section 251(c)(3), even temporarily.

It is true that agencies are entitled to substantial deference regarding interim relief. See MCI Telecommunications Corp. v. FCC, 750 F.2d 135, 140 (D.C. Cir. 1984). However, this deference is based on "the understanding that the agency may reasonably limit its commitment of resources to refining a rule with a short life expectancy." Competitive Telecommunications Ass'n v. FCC, 87 F.3d 522, 531 (D.C. Cir. 1996) (holding that FCC did not sufficiently justify an interim rate structure that had been in effect for years), enforcement denied, 1998 WL 135461 (D.C. Cir. Feb. 20, 1998) (denying enforcement due to transfer to Eighth Circuit). But nothing about the "interim" nature of the BOCs' proposal supports a rule that contradicts the Act.

The BOCs' proposal does not satisfy the requirements of Comptel.

First, though they are willing to defend their proposal only as a "provisional" measure, the BOCs' rule would not survive only for some limited time, but indefinitely, until there are no more implicit universal service subsidies in interstate access charges. Given the Commission's notable reluctance to date to take the necessary steps to complete universal service reform, see Texas Office of Public Utility Counsel v. FCC, No. 97-60421, 1999 WL 556461 (5th Cir. July 30, 1999), and the high likelihood that implementation of any Commission decision on universal service reform will be further delayed by an appeal made by an affected party, the BOCs' "temporary" rule could be in place for years. When that rule squarely contravenes its implementing statute, this is an unlawful state of affairs.

In contrast, the limited preservation of certain access charges for leased switched access services that were put in place in August 1996 as part of the Local Competition Order by regulation expired in June 1997. In upholding this regulation, the Comptel court relied on the fact that the transitional rule at issue was of brief and fixed duration. See Comptel, 117 F.3d at 1073 ("It is significant to our review for unlawfulness that the CLCC and TIC presently being assessed may be collected no later than June 30, 1997."). Similarly, in defending this rule, the Commission "strongly emphasize[d] that these charges will apply . . . only for a very limited period, to avoid the possible harms that might arise if we were to ignore the effects [of the rule on the] implementation of section 251." Local Competition Order ¶ 724. Indeed, the Commission found it to be "imperative that this transitional requirement be limited in duration," and stressed that it could "conceive of no circumstances under which the [transitional] requirement . . . would be extended further." Id. ¶ 725.

Second, the BOCs have not shown any need for their "transitional" rule, particularly in light of their success in denying the practical availability of extended links. In Comptel, the court upheld the Commission's ten-month transitional rule allowing non-cost-based "access" charges because of the Act's "nine-month disparity between the deadline for implementation of cost-based service and the deadline for reform of universal service." Comptel, 117 F.3d at 1074. Because the nine-month disparity raised "the threat of serious disruption in universal service," the court held that the transitional rule was appropriate "to effectuate [the universal service provisions] of the Act." Id.

The court, in other words, accepted the Commission's judgment that the limited 10-month rule enacted in the Local Competition Order was necessary because it had not had the opportunity even to begin to consider how it would "create a new system of funding universal system," and, given the ambitious six-month statutory time frame to promulgate rules to implement section 251, was unable to "take into account the effects of the new rules on our existing access charge and universal service regimes." Local Competition Order ¶ 716. In light of these concerns, and the "extraordinary upheaval in the industry's structure set in motion by the 1996 Act," id. ¶ 726, in response to BOC arguments that these brand new commercial arrangements threatened universal service funding, the Commission felt that prudence dictated that it apply a small part of the existing access charge regime to certain UNE leasing requirements for a 10-month period.

Now, however, the situation in Comptel that justified allowing traditional universal service principles to take precedence over the pricing standards of the 1996 Act no longer exists. The dates for implementation of sections 251, 252, and 254 of the Act have long passed, the universal service order has been entered, and the nine-month disparity between the local competition and universal service provisions has no continuing relevance. Today the Commission has had three years of experience under the 1996 Act. CLECs in particular have had the right for three years to lease unbundled elements exclusively for the provision of access services. Two years have passed since the end of the Commission's temporary imposition of access charges related to switched access. During these periods the arbitrage that the BOCs continue to claim will result from the application of the Commission's rules has not come to pass. In 1996 there was no empirical evidence upon which the Commission could rely and so it had no choice but to rely on its expert predictive judgment in formulating a provisional rule. Today there is such empirical evidence, though the BOCs for good reason have not provided it in their ex partes or elsewhere. If the practices the BOCs would have the Commission proscribe really presented tremendous opportunities for profitable entry, and if the CLECs really could as a practical matter take advantage of these opportunities, the market already would have experienced the changes the BOCs fear. In fact, there has been only the most minimal erosion of the BOC customer base, and that erosion has not made it difficult for the BOCs to meet their universal service obligations. The BOCs offer no evidence that this situation will change in the immediate future. This is reason enough to deny them the emergency relief they request.

Indeed, what the record reflects is that over the course of the last three years CLECs have faced and will continue to face formidable barriers to entry if they seek to enter any portion of the market through the use of unbundled network elements. Undeveloped OSS systems, untested operating rules and practices, rates not based on cost, and ILEC "slow-rolling" prevent CLECs from taking advantage of whatever opportunities exist on a scale that could promptly erode the ILECs' customer base. All of these problems apply to extended links. And even leaving all of that aside, in the case of dedicated access, much of the CLECs' business is governed by access contracts with the ILECs that contain substantial penalties if IXCs fail to meet volume and/or term commitments. Because of these contractual obligations, CLECs cannot overnight "convert" their dedicated access business to a business served by unbundled network elements.

The BOC provisional rule, in sum, is designed to address an emergency that the record establishes does not exist.

Third, the ostensible purpose of the rule is contrary to Commission policy. The BOCs claim (wrongly, we believe, see supra and infra) that the rule is necessary to preserve from rapid competitive assault cost structures that are grossly in excess of the true cost of the services provided, because it is Commission policy that these excessive costs be preserved until the completion of universal service reform. The Commission, however, has not adopted such a policy.

At the time of the Local Competition Order, the Commission had not yet decided how it would proceed to reduce access charges to cost; indeed, the very purpose of its limited transitional rule was to give it time to consider that and related questions. Today, however, the Commission has answered that question: rather than reduce access charges to cost solely by administrative fiat, the Commission has determined instead that it will promote competition for local and access services, in the hopes that competitive pressures of the market will lead to a reduction in access charges to cost. See First Report and Order, In re Access Charge Reform, 12 F.C.C.R. 15982, ¶ 48 (1997) ("Charge Reform Order") (intending to reduce access charges by "generat[ing] workable competition in the next several years"). See also id. ¶¶ 9, 35, 42. Competition from CLECs that use unbundled network elements to provide telecommunications services in competition with the ILECs is one of the types of competition on which the Commission was counting to drive access charges to cost. Obviously, a rule such as that proposed by the BOCs, whose very purpose is to deter competition in access services for the purpose of preserving supra-competitive access charges, is directly contrary to the Commission's stated policy of promoting competition to reduce access charges.

Fourth, the BOC rule is is so grossly underinclusive that it is not rationally related to the purpose to which it is allegedly directed. The rule purportedly is designed to preserve supra-competitive rates. But the critical element that supports services that are vastly overpriced (and over which the ILECs retain bottleneck control) is the loop, and yet the rule targets only extended link, leaving CLECs the unrestricted right to use unbundled loops solely for the purpose of providing access services.[4] If there really were a problem with arbitrage (and there is not), this proposed regulation would not solve it.

The proposed rule also is underinclusive in that the vast majority of access service, and so most of the income generated by access charges, is generated through switched access, not dedicated access. Yet the proposed rule targets only dedicated access. In support of their proposal, the BOCs rely almost exclusively on the fact that the Commission previously granted a 10-month provisional rule governing switched access. But this merely highlights the fact that the Commission has already determined that there was no reason to limit the uses made of elements to provide dedicated access, no doubt because such use accounted for so little or none of the revenues that allegedly constitute the implicit universal service subsidy. Indeed, it is "established Commission practice that special access will not subsidize other services," Access Charge Reform Order ¶ 404, a conclusion that is squarely at odds with the BOCs' assertion that they will not be able to meet their universal service obligations if special access prices are reduced to cost, unless the BOCs are suggesting that their current practices violate "established Commission practice."

[4]A rule that was actually designed to prevent CLECs from purchasing UNEs to offer access services would shut down the so-called data CLECs, such as Covad and Rhythms, that lease unbundled local loops to offer what the Commission has characterized as an access service. Indeed, depending upon how the BOCs would define "extended link," their proposal would have just that effect, at least in the many cases in which the data CLECs are forced to rely upon ILEC transport. And if the BOCs intend to draw a distinction in this regard between extended link in which the CLECs purchase collocation (which would not be covered by their limitation), and extended link that operates without the need to collocate (which would be covered), that distinction bears no relation at all to the preservation of access charge revenues. Instead, it is simply another attempt to force CLECs to purchase collocation, whether or not there is any real need for it.

Finally, in this regard, the rule is underinclusive (and discriminatory) in that it penalizes only those competitors for access traffic who lease ILEC extended link facilities, leaving access providers who supply their own transport but lease ILEC loops free to compete for access traffic without this limitation. Not only does this violate the Commission's sound conclusion that the Act is neutral as to the varies avenues for competition it creates, but it would also create artificial incentives to build transport facilities when it would otherwise be more efficient to lease them.

In sum, the BOC proposal is so unrelated to their claimed need to limit erosion of access charge revenue that it cannot rationally be supported by invoking such a need.

II. <u>The BOCs Rule Would Harm Competition And Be Bad Public Policy.</u>

Even if the BOCs' proposal were not unlawful, it should not be implemented because its effects would be harmful to consumers and to competition.

<u>First</u>, Congress wisely decided that when CLECs lease ILEC network elements, they should be able to make any use of them they see fit to provide competing telecommunications services. Under the BOC proposal, when CLECs lease ILEC elements, the ILECs would have the right to police the CLEC network to make sure the CLECs have the "right" kind of customers, and could (and no doubt would) strategically deny access to network elements based on purported concerns that CLECs were carrying "illegal" access traffic. There is no conceivable way to administer the rule the BOCs propose without creating endless opportunities for the ILECs to subject their CLEC competitors to anticompetitive rules and practices.[5]

[5]The recent Bell Atlantic extendalink tariff in New York ought to be a warning to the Commission as it considers the BOC proposals. Bell Atlantic requires a minimum of 50 percent local usage for this tariffed service, and indicates that it will require CLECs whose access traffic exceeds that percentage to collocate. This is an invitation for Bell Atlantic to police CLEC traffic in New York.

Second, because of the access pricing flexibility the Commission apparently intends to give to the ILECs, the BOC rule will give ILECs a license to engage in price squeezes that will cause great harm to the developing market for access services. In this context the BOC proposals amount to little more than a plea that they be allowed to offer access services at cost-based prices when it serves their interests, but that CLECs should be prevented from doing the same. It does not serve the public interest to allow the ILECs unilaterally to determine which customers should be required to pay inflated rates. While the BOCs suggest without any foundation that the Commission's rules will harm CAPS, the truth of the matter is that if the ILECs are given the pricing flexibility promised to them by the Commission, unless CAPS and CLECs retain the right to lease UNEs at cost-based rates, they will be unable to respond to the anticompetitive pricing that is the inevitable consequence of the new access rules.

Third, the BOC rule will deter facilities-based local competition just as surely as it will deter competitive service through unbundled network elements. As CLECs have explained in a series of ex parties to the Commission, their ability to use their own switching is greatly enhanced by the availability of extended link. Indeed, if the Commission were to adopt a rule in the instant proceeding that limited access to ILEC unbundled local switching, CLECs would become all the more dependent on extended link to extend the reach of their switches and gain access to customers. The BOC proposal is a dagger directed to the heart of this entry strategy: it would prevent CLECs from using leased facilities efficiently to carry all CLEC traffic to CLEC switches. The availability of extended link, as an economic matter, depends upon CLECs being able to make full use of the dedicated leased facilities they need to carry local traffic to their switches. The ILECs freely mix access and local traffic on their transport facilities. The CLECs, who have much less traffic to begin with, will be substantially disadvantaged if they are unable to do the same. In a business characterized by tremendous economies of scale, rules that artificially prevent CLECs from enjoying the benefits of whatever economies they can generate through their own business efforts will seriously deter the development of local competition.

In sum, the BOC proposal is bad policy as well as bad law.